

**Before the
Federal Communications Commission
Washington, DC 20554**

In the Matter of	§	
Review of Section 272(f)(1) Sunset of	§	
the BOC Separate Affiliate and Related	§	WC Docket No. 02-112
Requirements	§	

Comments of the Public Utility Commission of Texas

On May 24, 2002, the Federal Communications Commission (FCC) released a *Notice of Proposed Rulemaking* (NPRM) in the Matter of Review of Section 272(f)(1) Sunset of the Bell Operating Companies (BOC) Separate Affiliate and Related Requirements, WC Docket No. 02-112, FCC No. 02-148. In this NPRM, the FCC requests comment on whether the structural separation, nondiscrimination safeguards, and the biennial audit of BOCs established in section 272 of the Federal Telecommunications Act of 1996 (FTA) should be extended beyond the three-year sunset provision in the statute and, if so, what conditions, if any, should apply.

In order to better assess the statutory sunset, the FCC is interested in comments about the nature of the marketplace three years post-entry. In particular, the FCC asks whether competition has continued to develop in the states where section 271 applications have been granted and, if so, on which geographic areas or types of customers has that competition been focused. The FCC also seeks comments on (a) whether it should adopt a nationwide rule regarding sunset, or proceed on a case-by-case basis; and (b) whether viable alternatives to sunset are available, including less restrictive safeguards that do not require structural separation.

The Public Utility Commission of Texas (Texas PUC), having general regulatory authority over public utilities within our jurisdiction in Texas, submits these comments in response to the NPRM.

I. INTRODUCTION

The Texas PUC believes that the sunset or modification of the section 272 requirements on Southwestern Bell Telephone Company of Texas (SWBT) would at this time be imprudent and untimely given: (a) SWBT's continuing performance deficiencies in

providing access to competitors; (b) the lack of alternative access points to the network; and (c) the lack of access to SWBT's initial biennial audit. Accordingly, the Texas PUC strongly urges the FCC to extend SWBT's section 272 requirements for a minimum of one year past the July 10, 2003 and, preferably, until the second biennial audit of SWBT is completed and released by the FCC.

FTA section 271(d)(3) provides, in part, that the FCC shall not approve a BOC's 271 application for authority to offer in-region, interLATA services "unless it finds that . . . the requested authorization will be carried out in accordance with the requirements of section 272."¹ Clearly, Congress intended to establish a link between FTA sections 271 and 272. Moreover, by authorizing the FCC to extend section 272 requirements, Congress did not intend for such requirements to simply be "flash cut" three years after a BOC received 271 approval. Rather, the Texas PUC believes that the section 272 requirements were established to simultaneously monitor the BOCs relationship with its long distance affiliate, while fostering the emerging competitive market.

To implement section 272, the FCC created a set of nondiscrimination safeguards designed to discourage and detect improper cost allocation and cross-subsidization between a BOC and its affiliate.² As the FCC stated in the NPRM, the safeguards were an acknowledgement that the BOCs have market power in the provisioning of local exchange and exchange access services in their respective service areas.³ The NPRM further states that "as long as the BOCs retain market power in the provision of these services, they will have an incentive and ability to discriminate against their long distance competitors, and engage in other anti-competitive conduct."⁴ As the FCC stated in the order approving SWBT's Texas

¹ 47 U.S.C. § 271(d)(3).

² See *Implementation of the Accounting Safeguards Under the Telecommunications Act of 1996*, CC Docket No. 96-150, Report and Order, 11 FCC Rcd 17539 (1996) (*Accounting Safeguards Order*), Second Order On Reconsideration, FCC 00-9 (rel. Jan. 18, 2000); *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905 (1996) (*Non-Accounting Safeguards Order*). The safeguards are codified at 47 C.F.R. §§ 53.1 – 53.213 (2001).

³ NPRM at 3, citing *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905, 21911-12.

⁴ NPRM at 3.

271 Application, “compliance with section 272 is ‘of crucial importance’ because the structural, transactional, and nondiscrimination safeguards of section 272 seek to ensure that BOCs compete on a level playing field.”⁵

The Texas PUC believes that although some progress has been made toward leveling the field, SWBT’s continued dominance over local exchange and exchange access services still hinders the development of a fully competitive market, especially given the current status of the financial markets, competitive local exchange carriers (CLECs) access to capital, and the bankruptcy of many competitive carriers. Thus, SWBT retains both the incentive and ability to discriminate against competitors and to engage in anti-competitive behavior. Furthermore, the initial biennial audit of SWBT, as required by section 272(d), has not yet been released by the FCC. As a result, the Texas PUC cannot represent that circumstances in Texas’ markets warrant removal of competitive safeguards.

In summary, the Texas PUC maintains that removal of the separate affiliate requirements at this time would fail to meet Congress’ objectives in implementing section 272. Additionally, if the section 272 requirements are sunset, Texas and the FCC will lose a valuable means to ensure SWBT’s compliance with its obligation to provide access to the local exchange and exchange access markets that SWBT controls. Accordingly, prudence demands that the sunset period be extended until the conditions which necessitated the creation of competitive safeguards no longer exist. At a minimum the sunset period for SWBT in Texas should be extended an additional year beyond the current sunset date (July 10, 2003), and, preferably until completion and release of the second biennial audit.

II. COMPETITION IN THE LOCAL MARKET

As part of its assessment of the statutory sunset, the FCC seeks comment on the nature of the marketplace three years post-entry, and the condition of competition in states where section 271 applications have been granted.⁶ The Texas PUC supports examining the

⁵ *Application by SBC Communications Inc, Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Texas*, CC Docket 00-65, Memorandum Opinion and Order, ¶ 395 (rel. Jun. 30, 2000), *quoting Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended*, CC Docket No. 97-137, 12 FCC Rcd 20543, 20725 (1997).

⁶ NPRM at ¶ 12.

condition of the local marketplace three years post-entry and believes that the state of affairs in the local market provides the best context in which to assess whether the separate affiliate safeguard provisions for competitive activities are still needed.

The intent of the FTA's existing structural safeguards was to provide adequate opportunity and time for competition to develop in all markets (e.g., local exchange and exchange access) and to prevent BOCs from discriminating against others in favor of their affiliates. In particular, Congress acknowledged that, while the local exchange market may not be fully competitive upon its opening, competitors would enter the market and become alternative sources for local exchange and originating access services. This, in turn, would curtail the ability of BOCs to discriminate against competing providers of interexchange service.

While it has been over six years since the passage of the FTA, the FCC has only approved section 271 applications in 15 states. The Texas PUC urges the FCC to consider this lack of broader 271 approval nationwide as a strong indication that the majority of markets are not sufficiently open to allow competitors access to the local market. Even in states with section 271 approval, competition is still emerging, especially in the residential market, and many competitors are struggling to remain financially viable. As is true across the nation, in Texas, a considerable number of carriers have either exited the marketplace or appreciably reduced the areas in the state in which they provide services.⁷

In Texas, where SWBT was granted entry into long distance over two years ago, CLECs still serve only 16% of the business and residential access lines in Texas as of June 30, 2001.⁸ For 1999, the Texas PUC reported that CLECs had only 13.6% percent of the local marketplace.⁹ Moreover, the competition that does exist in Texas relies heavily on UNE-P as

⁷ In Texas, over 41 CLECs have filed for bankruptcy protection since 2001. *PUC Proceeding for Filing Bankruptcy Notification(s) by COA and SPCOA Holders*, Texas PUC Docket No. 23998 (April 20, 2001). According to BankruptcyData.com, over 63 telecommunications company have filed for bankruptcy protection nationwide.

⁸ *Local Telephone Competition: Status as of December 30, 2001* at Table 7, Industry Analysis Division, Common Carrier Bureau, Federal Communications Commission (July 2002).

⁹ *Report to the Legislature on the Scope of Competition in Telecommunications Markets of Texas*, Texas PUC No. 21167 at 38-41 (Jan. 2001) (a disproportionate amount of CLEC lines are in the business market in large metropolitan and suburban areas).

an entry mechanism.¹⁰ During the period January 2000 to June 2001, UNE-P accounted for more than 88% of the net gain in competitive activity in Texas.”¹¹

Accordingly, the Texas PUC believes that the separate affiliate safeguards afforded by section 272 should remain in place until the local marketplace is more competitive. The Texas PUC believes that maintaining such requirements will afford the necessary market certainty to foster the continued development of competition in the local, long distance and information services markets as envisioned in the FTA.

III. ACCESS TO SWBT’S LOCAL AND LONG DISTANCE NETWORKS

Given the link between sections 271 and 272, the Texas PUC believes that SWBT’s treatment of competitors in the local market does not warrant sunset of the section 272 requirements at this time. The Texas PUC believes that creating a level playing field among competitors in the telecommunications market when one competitor owns the network and provides access to other competitors to allow them to compete, is still compelling today, especially given the current market conditions. Further, since the passage of the FTA, BOCs have been granted section 271 authority and have entered the long distance market, increasing their incentive to act in an anticompetitive manner against competitors in both the local and long distance markets.

Further, current proceedings pending at the Texas PUC involve issues of special access and discriminatory treatment.

A. Local Access:

The Texas PUC finds that, two years after receiving 271 approval, SWBT continues to fail to achieve full compliance with Texas’ performance measures (PMs). During the collaborative process that lead to the Texas PUC’s support of SWBT’s section 271 application, the PMs were established to assess SWBT’s performance in opening local markets to competition. The PMs were designed to identify problems and improve SWBT’s

¹⁰ See Notice of Proposed Rulemaking in the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, CC Docket No. 01-338, Comments of the Public Utility Commission of Texas, Table I, Importance of UNE-P in Texas, page 5-6. (May 10, 2002).

¹¹ *Id.* at 6.

procedures and behavior toward CLECs. The PMs are reviewed every six months to ensure SWBT's compliance and to modify, delete, or add measures, as needed, to more accurately capture data tracking SWBT's performance.

From November 1999 to the present, SWBT has paid over \$23 million in Tier 1 and Tier 2 damages to other carriers and the State of Texas, respectively. Additionally, in the six months from November 2001 through April 2002 (the date of the most recent data), SWBT had over 525 separate violations, although not all resulted in fines. Without addressing the merits of the violations and the relative fines, the fact is that there does not appear to be a significant trend downward in either category. Apparently, while the establishment of performance measures theoretically disincentivizes anti-competitive and/or discriminatory behavior, the Texas PUC has not documented this intended effect on SWBT's performance. Accordingly, the Texas PUC believes that if the section 272 requirements are allowed to sunset, Texas is at risk of losing its only statutory means of monitoring SWBT's obligation to provide access to its network.

B. Long Distance Access:

1. Proceedings at the Texas PUC relating to allegations of discriminatory access

In response to the FCC's request, the Texas PUC has identified at least two cases that may indicate that problems still exist in providing access to the networks, two years after approval of SWBT's section 271 application. In a recent arbitration proceeding at the Texas PUC, the arbitrators found that SWBT was refusing to allow CLEC customers to presubscribe to SWBT's intraLATA toll service. The arbitrators found such actions to be a clear violation of existing state law and the FTA's pro-competitive policies, and therefore ordered SWBT to provide toll service on a nondiscriminatory basis.¹² Also pending before the Texas PUC is a complaint filed by a competing long distance carrier alleging that SWBT, since receiving 271 approval in Texas, has engaged in intra-corporate, cross-subsidization practices with its long distance affiliate that have enabled it to engage in price squeezes for interLATA and

¹² *Petition of MCIMetro Access Transmission Services, LLC, Sage Telecom, Inc., Texas UNE Platform Coalition, McLeod USA Telecommunications Services, Inc. and AT&T Communications of Texas, L.P. for Arbitration with Southwestern Bell Telephone Company under the Telecommunications Act of 1996*, Docket No. 24542, Arbitration Award at 201-203 (May 1, 2002). The Texas PUC Commissioners presided over the Arbitration, and found that SWBT is obligated under PURA § 55.009(c) to allow CLEC local service customers to presubscribe to SWBT as their intraLATA toll carrier.

intraLATA telecommunications services that are anti-competitive, predatory, unreasonably preferential and discriminatory.¹³

2. Special Access Arbitration in Texas

Given SWBT's performance regarding Texas' PMs, the section 272 requirements take on greater importance as a mechanism for compelling SWBT to open up its markets to competition. This is especially true given the fact that exchange access, or special access, and the monitoring thereof, is vital to competition in both the local and long distance markets. The Texas PUC is arbitrating a dispute regarding the appropriateness of mandating special access performance measures to ensure that SWBT provides long distance competitors with parity access to the network.¹⁴

The *Texas Special Access Arbitration* arose out of a Texas PUC workshop in the section 271 compliance monitoring docket of SWBT.¹⁵ In the workshop, CLECs complained that they were being forced to order from SWBT's special access tariff in order to complete their local networks. Cited examples included having to order special access due to the unavailability of Unbundled Dedicated Transport or the lack of loop capacity; and SWBT's refusal to combine unbundled network elements with special access.¹⁶

Similarly, as noted in the NPRM, the FCC is currently considering adoption of measures and standards for interstate special access services.¹⁷ Given that special access involves the provisioning of both intra and interLATA communications, thereby raising questions of joint federal/state jurisdiction, there is considerable potential for delay and confusion, leading to heightened uncertainty. Until these matters are resolved, the separate affiliate requirements of section 272 remain the most effective means of assessing the BOCs'

¹³ *Complaint of AT&T Communications of Texas, L.P. against Southwestern Bell Telephone Company and Southwestern Bell Communications Service, Inc. d/b/a Southwestern Bell Long Distance* at 2-3, Docket No. 23063 (Sept. 22, 2000) (pending).

¹⁴ *Petition of Southwestern Bell Telephone Company for Arbitration Regarding the Implementation of Special Access Performance Measures*, Docket No. 24515, Aug. 17, 2001 (pending) (*Texas Special Access Arbitration*).

¹⁵ *Section 271 Compliance Monitoring of Southwestern Bell Telephone Company of Texas*, Texas PUC Docket No. 20400, Transcript from Workshop (April 5, 2001).

¹⁶ *Id.* at p. 464-68.

¹⁷ NPRM at ¶ 26.

compliance with the statutory obligation to not discriminate against other entities in favor of its affiliates.

IV. BIENNIAL AUDIT

The initial biennial audit has not been released by the FCC, and therefore sunset of the competitive safeguards is, at a minimum, premature given that the Texas PUC has not had an opportunity to evaluate or comment on the initial audit. Pursuant to FCC rules, the initial biennial audit of a BOC's relationship with its long distance affiliate is performed on the first full year of operations of the affiliate.¹⁸ SWBT's first audit covered the period from July 10, 2000 to July 9, 2001, and was initiated mid-way through the first year SWBT began offering interLATA services in Texas. Moreover, should the initial audit raise questions regarding the audit procedures, or evidence a pattern of discriminatory behavior or cost misallocation, such matters would need to be addressed and remedied in the second biennial audit. The second audit, which will cover the period from July 10, 2001 through July 9, 2003, is scheduled to begin in the near future and will not likely be completed and released until 2004.

As an option, the Texas PUC proposes that the FCC extend SWBT's section 272 requirements for a minimum of one year, thus synchronizing the 3 year sunset period in section 272(f)(1) (regarding manufacturing and long distance) with the 4 year period set out in section 272(f)(2) (regarding interLATA information services). This would allow for a comprehensive compliance evaluation to take place simultaneously, rather than on a piecemeal basis. However, even after the first audit is released, relying thereon to determine whether or not to sunset competitive safeguards would be to place too much reliance upon a single audit, especially given the inherent shortcomings of auditing an evolving company in a developing market.

The Texas PUC's preferred option, however, is to extend SWBT's section 272 requirements until the completion and release of SWBT's second biennial audit. While the initial audit covers the first year of operations for SWBT's long distance affiliate, it reflects a company that was still developing its operational procedures, was entering a new marketplace, and was experiencing the growing pains of any new company. As a result, the

¹⁸ 47 C.F.R. § 53.209(c).

auditors did not have a historical perspective with which to compare the operations of the affiliate vis-à-vis SWBT. SWBT's second audit will address the activities of a more mature affiliate, and one which has now been activated in an additional three SWBT states. Further, the second audit will allow for the implementation of remedial measures and monitoring of any problems and issues identified in the first audit. Therefore, without reviewing both audits, it is impossible to fully assess whether the Congressional mandates of section 272 have been satisfied. Moreover, an extension would give the FCC and the Texas PUC time to evaluate the need for, and develop, an alternative compliance mechanism to ensure that the nondiscriminatory provisions of section 272 which do not sunset (i.e., sections 272(e)(1) and (4)) are complied with by SWBT.

V. ALTERNATIVES

In the NPRM, the FCC proposes several alternatives to allowing the section 272 requirements to sunset.¹⁹ Three of these alternatives involve the sunset of the separate affiliate requirement and retention, in some form or other at either the federal or state level, of the statutory safeguards and/or biennial audit.²⁰ Section 272, however, is premised upon requiring the BOCs to have a structurally separate affiliate through which they offer interLATA services. Similarly, the nondiscrimination safeguards and biennial audit provisions presuppose the existence of a separate affiliate and are specifically directed at the relationship between the BOCs and such affiliate. While the Texas PUC has not done an exhaustive legal analysis of section 272, the plain language of the statute would seem to indicate that a sunset of the separate affiliate requirement would result in a sunset of the safeguards and biennial audit. Accordingly, if structural separation is allowed to sunset, giving effect to the safeguard and audit provisions would require imposition of these requirements on the BOCs themselves, which appears to go beyond the plain language of the statute. Moreover, examining alternatives is premature and imprudent until such time as the viability of the competitive marketplace has stabilized and there are assurances that the competitive safeguards are no longer necessary.

¹⁹ NPRM at 7-10.

²⁰ *Id.*

VI. CONCLUSION

The Texas PUC appreciates the opportunity to comment on the FCC's NPRM, and to assist the FCC in developing long-term solutions to the issues addressed. The Texas PUC strongly urges the FCC to extend SWBT's structural separation and related requirements under section 272 a minimum of one year beyond the current sunset date, and preferably, until after completion and release of SWBT's second biennial audit.

Respectfully submitted,

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July 25, 2002

/original signed/

**Rebecca Klein
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**Brett A. Perlman
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